88-1402

Supreme Court, U.S.
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JOSEPH F. SPANIOL, JR.
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No.

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1984

BERNARD J. FLAYAC, Petitioner,

v.

CRAIG HUMRICHOUSE, et al., Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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QUESTIONS PRESENTED

1. Should the Supreme Court reconcile the differing standards between the Ninth Circuit Court of Appeals, on the one hand, and the Eighth Circuit Court of Appeals, on the other, as to which evidence may be considered in granting a motion for direct verdict or judgment?

2. Does the statistical imbalance of cases reaching trial between the Ninth Circuit Court of Appeals and the Eighth Circuit Court of Appeals, arising from this differing standard, constitute a denial of right to jury trial available to parties bringing cases within the Ninth Circuit Court of Appeals?

LIST OF PARTIES

The parties to the proceedings are the Petitioner, BERNARD J. FLAYAC, a French national, GARY HUMRICHOUSE, CRAIG HUMRICHOUSE and DAVID WITT, Atlantic Richfield AM/PM Mini-Market franchisees, JAMES J. SCHWARTZ, Mr. Flayac's prior California, and HAINS, WALKER & SCOTT, the attorneys for Messrs. Humrichouse and Witt.

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OPINIONS BELOW

The opinion of the Court of Appeal for the Ninth Circuit is unreported, but is reprinted in the appendix hereto at page 1A, infra.

A motion for rehearing was timely filed, and denied. The instant Petition for Certiorari is filed within ninety (90) days of the date of that denial.

JURISDICTION

The District Court has subject matter jurisdiction pursuant to 28 USC Section 1332(a)(2) (diversity jurisdiction), in that BERNARD J. FLAYAC is a citizen of France and the amount in controversy is in excess of Ten Thousand Dollars ($10,000.00).

COURT OF APPEALS JURISDICTION

The Court of Appeals has jurisdiction pursuant to 28 USC Section 1291 in that the appeal is from a final judgment of the District

Court, which disposed of all claims of the parties.

This Petition is filed within ninety (90) days from date the petition for rehearing was denied by the Ninth Circuit Court of Appeals, pursuant to 28 USC Section 2101(c).

RULE INVOLVED

Federal Rule of Civil Procedure 50A, motion for a directed verdict and for a judgment notwithstanding the verdict (a) motion for a directed verdict: when made: effect. A party who moves for a directed verdict at the close of the evidence offered by an opponent may offer evidence in the event that the motion is not granted, without having reserved the right so to do and to the same extent as if the motion had not been made. A motion for a directed verdict which is not granted is not a waiver of trial by jury even though all parties to the action have moved for directed verdicts. The motion for a directed verdict shall state the specific grounds therefor. The order of the court

granting a motion for a directed verdict is effective without any assent of the jury.

STATEMENT OF THE CASE

BERNARD J. FLAYAC is a French national currently residing in the United States under a treaty investor's VISA (E-2 VISA), issued by the United States Department.

At all times relevant to the instant dispute, Mr. Flayac had only a minimal ability to either comprehend or speak English, had become and had been a resident of the United States for less than a month, and was unfamiliar with role of American attorneys in business transactions. In the District Court, Mr. Flayac testified that in France, it was the custom for both the buyers and sellers to use only one attorney to represent parties in a business transaction.

In December of 1983, Mr. Flayac visited a friend, Jean-Pierre Turteaut to investigate the possibility of investing in or buying a small business in the San Francisco area.

Unhappily for Mr. Flayac, Mr. Turteaut introduced him to a business broker who, in turn, introduced Mr. Flayac to Gary Humrichouse, Craig Humrichouse and David Witt, owners of three AM/PM Mini-Marts in the town of Livermore, California (hereinafter the "Humrichouse Defendants").

The Humrichouse Defendants were the franchise owners of these stores pursuant to written contracts with the Atlantic Richfield Company (hereinafter "ARCO").

Following negotiations, Mr. Flayac made a written offer to pay $1,300,000.00 for the purchase of these three gas stations.

Consummation of the sale was expressly conditioned on the parties obtaining the "approval" by ARCO of the transfer of the franchises from the Humrichouse Defendants to Mr. Flayac. ARCO's franchising policy was that no franchisee could transfer or sell a station franchise except with the prior written consent or approval of ARCO. The conditional purchase by Mr. Flayac encountered the imposition of two

distinct policy requirements for ARCO respecting their franchisees: first, ARCO had a "one owner, one store" policy, which ARCO would not knowingly consent to a single individual owning more than one station; secondly, ARCO had a requirement that any AM/PM Mini-Market franchisee be either a United States citizen or have a "permanent residence".

To avoid technical application of the "one owner, one store" policy, and at the suggestion of the Humrichouse Defendants, Mr. Flayac designated his friend Mr. Turteaut and the business broker in the transaction as separate applicants for two of the stores. Mr. Turteaut and the business broker were only "stand-ins" for Mr. Flayac, who was at all times to be the real owner of the stores.

The fact that Mr. Flayac was to be the real owner was made known to all of the parties, including Mr. Flayac's lawyer, James J. Schwartz (hereinafter "Schwart"), and Hains, Walker & Scott, lawyers for the Humrichouse Defendants (hereinafter "HW&S").

Three separate escrows for the sale of the stores were set up by the parties, with Mr. Flayac, Mr. Turteaut and the business broker as buyers, and Gary Humrichouse, Craig Humrichouse and David Witt as the sellers. However, there was a fourth escrow document drawn up by Hains, Walker & Scott for submission to ARCO. This document appointed Hains, Walker & Scott as escrow agents for the sale of one of the stores.

The reason this fourth escrow document was necessary was that, pursuant to ARCO policy, each of the sellers needed to be separately licensed by the California Alcoholic Beverage Control Board of the State of California. On ARCO's books, each of the sellers licensure was so reflected. In fact, however, two of the stores were licensed to David Witt, as Gary Humrichouse could not qualify for a license, having been convicted of child molestation. These facts were unknown to Mr. Flayac or to ARCO.

The Humrichouse Defendants, and their lawyers, realized that twice as much was being

paid for these stores as they were worth. They were afraid ARCO would not approve the transaction. Therefore, half of the money was paid "under the table" to the sellers through a Hains, Walker & Scott Trust Account in the Bank of Livermore set up specifically for this transaction. At some point in the transaction, ARCO got wind of the deception being practiced upon it and disallowed and disapproved Mr. Flayac as a franchisee, on the ostensible ground that an E2 Treaty Investor VISA did not constitute a permanent resident document.

One of ARCO's lawyers telephoned Mr. Schwartz to inform him of Mr. Flayac's disapproval before the money had changed hands. On that day, Mr. Schwartz called Hugh Walker, one of the Humrichouse Defendants' attorneys, who immediately transferred the "under the table money" out of the Trust Account for the benefit of his clients. Mr. Schwartz allowed the transaction to proceed, and to be consummated, without ever insuring that ARCO approved his client as a franchisee, or without setting up

security devices to protect his client's investment in the event that ARCO did not give its consent.

After these facts had been presented to a jury, the Honorable Charles A. Legg granted, sua sponte, his own Federal Rule of Civil Procedure 50A motion, taking the case away from the jury.

The Ninth Circuit split two to one on the issue as to whether this directed verdict was proper. The Court is invited to read the assent of Circuit Judge Fletcher, which is annexed hereto as Exhibit "A". Quoting in part Judge Fletcher, she indicates:

> "I think it is obvious that the District Court erred in taking from the jury the question of Schwartz' liability for negligent representation. Further, the Court erred in thinking that Flayac derived any benefit from the Rincon store."

REASONS FOR GRANTING THE WRIT

It is difficult to believe that a French national can, in good faith, come to this country to invest his money, be bilked of it by

the machinations of a child molester and the negligence of attorneys he retained to protect him, and find no redress in our Court system. It is more explicable, however, when set against the stark statistical backdrop of the following facts: between the years of 1970 and 1987, the percentage of cases reaching trial in the Ninth Circuit District Court dropped from 7.6% to 2%, a decrease of 253%. Further, the percent of non-jury trials dropped from 6% to 2%, a reduction of 300%.

The average percentage of cases reaching the trial stage during that same 17-year period was 4.98% in the Ninth Circuit.

The Eighth Circuit, however, during that same period, saw 7.48% of its cases reach the trial stage, a 210% difference.

The reductions in trial activity occurred at a time when the number of cases coming before the District Courts in the Ninth Circuit jumped from 10,368 to 39,337, an increase of 379% (source, Annual Report of the Directors of the Administrative Offices of the United States

Court, 1987).

It is respectfully submitted that the statistical imbalance between the Eighth Circuit and the Ninth Circuit is created, at least in part, by the differing standards between the circuits in considering grant of motion for directed verdict pursuant to Federal Rule of Civil Procedure 50A.

If this reviewing Court will carefully read the analysis of the majority, the majority heavily relies upon the evidence presented by the Humrichouse Defendants and, this is consistent with the Ninth Circuit holding in Uniform Oil Company v. Phillips Petroleum Company, 400 F.2d 267 (9th Cir. 1983), which provides that the Ninth Circuit may consider all of the evidence at trial in granting or denying a motion for a directed verdict.

In the Eighth Circuit, however, the standard is different. As the Eighth Circuit held in the case of Dace v. ACF Industries, Inc., 72 F.2d 374 (8th Cir. 1983):

> "Our precedence predominately supports the general proposition that only the

> evidence favoring the non-moving party should be considered." Dace, at 376.

The Dace precedence has been recently followed in the Eighth Circuit in the case of Cochran v. Taylor, et al., 830 F.2d 900 (1987), at 902, 903, cert.den. 108 SC 1476 (1988).

Dace goes further, however:

> "We have recently stated flatly that on a motion for a directed verdict 'any evidence produced by the prevailing party must be disregarded'... That statement necessarily implies that evidence favorable to the moving party may not be considered, because if it were the Court would have to pass on the credibility of the parties' witnesses." [Emphasis added] Id, at 376.

The Ninth Circuit not only considered, for example, Hains, Walker & Scott's evidence, but they accepted it. One example is found on page 8 of the opinion below. Hains, Walker & Scott sought to exonerate itself from liability for having fabricated the fourth escrow document with testimony to the effect that, in a letter, they had asked the Humrichouse Defendants whether they wished to proceed with the escrow, but the Humrichouse Defendants had never

responded. However, the escrow document was sent to ARCO, and accomplished the deceptive purpose in an attempt to accomplish the deceptive purpose for which it was designed. The exonerating evidence of Hains, Walker & Scott was accepted, but Flayac's evidence wholly ignored.

The United States Constitution guarantees every citizen (and, for that matter, every foreigner suing in the United States Federal Courts) the right to a jury trial.

Due to the application of differing evidentiary standards in assessing Federal Rules of Civil Procedure 50A motions, Mr. Flayac's odds in reaching the jury in the Eighth Circuit would have been two to one better than those he received in the Ninth Circuit.

The statistical imbalance between cases reaching trial in the Eighth Circuit and the Ninth Circuit makes the administration of Federal Rule of Civil Procedure 50A an important procedural issue, as noted in Supremeourt Practice, Sixth Edition, by Robert L. Stern, at

page 220, by Stern, Gressman & Shapiro, in that work's discussion of Rule 17.1(a):

> "Rule 17.1(a) also recognizes the appropriateness of grant of certiorari in this type of case where the Federal Appellate decision has 'so far departed from the accepted usual course of judicial proceedings, or so far sanctions such a course by a lower court', as to call for an exercise of this Court's power of supervision."

In Justice Steven's words:

> "As the court of last resort in the Federal system, we have supervisory authority and, therefore, must occasionally perform a pure error correction function in Federal litigation." Supreme Court Practice, at p. 220.

CONCLUSION

The fact that Federal District Court litigation has proliferated in the Ninth Circuit should not permit Federal judges to defacto amend the Constitution by truncating a plaintiff's right to a jury trial. At least, if Federal Rule of Civil Procedure 50A is to be

fashioned into such broad a sword, it should be swung with equal weight between the circuits.

Dated: January 3, 1989.

Respectfully submitted,

McNICHOLS, McCANN & INDERBITZEN

By: _____
William D. McCann
Attorneys for Petitioner

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

BERNARD FLAYAC, Plaintiff-Appellant v. CRAIG ALLEN HUMRICHOUSE, et al., Defendants. and JAMES G. SCHWARTZ, individually; STALEY, YOUNG & SCHWARTZ, a professional corporation; HAINES, WALKER & SCOTT, a law partnership, Defendants-Appellees	No. 87-1553 D.C. No. CV-85-1363-CAL MEMORANDUM*

Appeal from the United States District Court
for the Northern District of California
Charles A. Legge, District Judge, Presiding

Argued and Submitted December 16, 1987
San Francisco, California

Before: FLETCHER, WIGGINS, NOONAN,
Circuit Judges

*This disposition is not appropriate for publication and may not be cited to or by the

courts of this circuit except as provided by 9th Cir. R. 36-3.

Flayac appeals from a directed verdict in favor of the defendants, Schwartz and the law firm of Haines, Walker & Scott (HW&S). Flayac brought attorney malpractice claims against Schwartz. He charged HW&S with a breach of fiduciary duty under escrow and trustee theories. We AFFIRM.

STANDARD OF REVIEW

In determining the propriety of a directed verdict the court of appeals has the same role as the court below. Othman v. Globe Indemnity Co., 759 F.2d 1458, 1463 (9th Cir. 1985). In reviewing a directed verdict, the court must view the evidence in the light most favorable to the nonmoving party and draw all possible inferences in favor of that party. Blanton v. Mobil Oil Corp., 721 F.2d 1027, 1219 (9th Cir. 1983), cert. denied, 471 U.S. 1099 (1985). A directed verdict is proper when the evidence permits only one reasonable conclusion as to the verdict. Peterson v. Kennedy, 771 F.2d 1244, 1256 (9th Cir. 1985), cert. denied,

475 U.S. 1122 (1986).

BACKGROUND

The appellant, Bernard Flayac, is a French national who owns various business in Asia and Africa. In late 1983 and early 1984, Flayac began to look for business opportunities in the United States. Flayac contacted a friend named Turtaut to help him. Turtaut, in turn, contacted Lynn Caudle, a licensed "business opportunity broker", who held himself out as a "service station specialist". In January, 1984, Flayac met with Gary Humrichouse, Craig Humrichouse and David Witt (Humrichouses) about the purchase of three ARCO AM/PM mimimarts from the Humrichouses. The Humrichouses accepted an offer of $1.3 million for the sale of the three stores. All the negotiations between Flayac and the Humrichouses regarding purchase price, their acceptance of his offer, the decision to have three separate applicants file for franchises, and the creation of several escrow accounts were completed before defendant Schwartz was retained

as Flayac's counsel. The offer to purchase the three stores was made subject to ARCO's approval of Flayac as franchisee.

Thus, in order to consummate the sale, the parties had to obtain ARCO's permission for the transfer of the franchises. The deal, as contemplated by the parties, violated two ARCO requirements. First, ARCO had a "one owner, one store" policy under which ARCO would not allow a single person to own more than one AM/PM. Second, ARCO required that its franchisees either be U.S. citizens or have permanent resident status. Flayac did not possess permanent residence status when he dealt with the Humrichouses or applied for a franchise with ARCO.

In order to circumvent ARCO's "one owner, one store" policy, Flayac had Caudle, Turtaut and himself separately fill out the franchise applications. Flayac also pursued the residency issue with ARCO. He, along with Turtaut and Caudle, had an interview with various ARCO representatives as part of the overall ARCO

approval process. Caudle was approved as franchisee of one of the stores (Rincon). Flayac was told that except for the residency requirement he and Turtaut otherwise qualified for the franchises.

On March 6, 1984, Flayac met with Schwartz. On the same date, Flayac purchased three CD's at a local bank in the aggregate amount of $730,000. Seven hundred thousand dollars of this money represented part of the purchase price of the three stores. One CD was purchased in the amount of $350,000 in the name of Flayac. The other two, in the amount of $190,000 each, were made out to Turtaut and Caudle. They immediately endorsed the CD's to Flayac. On March 13, 1984, Flayac directed the CD's to be paid into an HW&S trust account for the benefit of "GCD Investments, Inc." The trust account was an account created by HW&S for its long-term clients, the Humrichouses. Neither Schwartz nor HW&S was aware of the mechanics of this transaction until after it was completed.

On April 3, 1984, Flayac deposited some $635,000 in three different escrow accounts at Wells Fargo Bank. On April 14, 1984, Flayac called Schwartz and told him that Flayac had learned from Gary Humrichouse that ARCo had not approved Flayac's franchise application because he did not possess permanent resident status. On April 16, 1984, the parties signed an agreement, prepared by Schwartz, designed to circumvent the ARCO requirement. It was drafted to give Flayac the right to participate in the management and profits of the three stores even though he did not hold "legal" title to them. It also authorized disbursement of the $700,000 in the HW&S trust account to the sellers. The agreement provided that if ARCO failed to give its approval to Flayac and Turtaut as franchisees, then the Humrichouses would convert each store into a separate corporation and issue Flayac 49% of the stock in each corporation. The agreement, however, did not give Flayac any absolute right to the return of his money in the

event ARCO never approved the transfer.[1] On April 17, 1984, the Humrichouses met with HW&S and directed that the money previously endorsed to them be released from the GCD trust account. As per the unequivocal terms of the GCD trust account, they had an absolute right to disbursement of these funds any time after their deposit in the account. On April 17, 1984, Schwartz contacted ARCO's head in-house counsel, Fillmore Wood, and Wood confirmed that Flayac's application had been denied. Schwartz received a letter from Wood on April 30, 1984, officially rejecting Turtaut's and Flayac's applications. Schwartz told Flayac that ARCO found a residency problem with Flayac and Turtaut's applications.

The parties, including the attorneys for both sides, met on April 30, 1984 to discuss the residency problem. At the April 30 meeting, the Humrichouses mentioned the existence of a

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[1]It is the April 16 agreement prepared by Schwartz, and its failure to provide for the return of Flayac's $700,000, that provided the basis of the trial court's holding that Flayac had established a prima facie negligence claim against Schwartz.

corporation called "Howard Arlen, Inc.", a "holding" company that the Humrichouses primarily used for tax purposes in relation to the three stores. Schwartz prepared the first draft of an agreement to transfer Howard Arlen to Flayac. Schwartz sent the draft agreement to HW&S on May 3, 1984. The draft provided that the escrow accounts at Wells Fargo containing the $635,000 remain open until ARCO approved Flayac and Turtaut as franchisees. On may 4, 1984, Schwartz left on vacation (he returned on May 21, 1984). Schwartz' draft was revised by HW&S. The new version did not specifically refer to how long the escrows were to remain open, but did provide that they were to remain open. The Humrichouses and Flayac then met without their attorneys and changed the HW&S draft by cancelling the escrows. The new agreement further provided that the cancelled escrows would be "re-opened" and remain open until Flayac qualified with ARCO.

On May 16, 1984, the Wells Fargo escrow accounts were cancelled and the money returned

to Flayac. Flayac then immediately paid the balance of the purchase price outside of escrow by endorsing the checks for the escrow funds over to the Humrichouses. At this point, Flayac had paid the Humrichouses the entire $1.3 million purchase price for the three stores. Sometime later a "receipt" for the amount of $804,500 was signed by the Humrichouses acknowledging "payment" by Flayac for the transfer of Howard Arlen, Inc.

Prior to trial, the judge precluded admission of any evidence of a conspiracy between Schwartz and HW&S to defraud Flayac. At the close of the appellant's case-in-chief the trial court grant the appellee's motions for directed verdict. It ruled that HW&S owed Flayac no duty, as a matter of law, under either escrow or trustee theories.

The court further fund that there was sufficient evidence against Schwartz to go to the jury on the April 16, 1984 agreement. However, the Court, as a matter of law, found no liability in Schwartz for events that occurred

after he went on vacation. The court precluded any liability in Schwartz for losses incurred by Flayac arising out of the May 15, 1984 agreement. Thus, Schwartz' potential liability was limited to the $700,000 to the Humrichouses on April 17, 1984. The court set off any potential liability in Schwartz by $650,000 -- the face amount of a settlement previously entered into between Flayac and the Humrichouses. The court also set off any recovery against Schwartz by the purchase price ($350,000) of the Rincon store because Flayac had taken delivery of it. Flayac stipulated that the trial court might then enter directed verdicts on the entire case while preserving the right to appeal all issues. Appellant timely appealed.

ANALYSIS

I. Haines, Walker & Scott.

The appellant argues that HW&S is liable to Flayac for breach of its duty as an escrow agent. Flayac points to a set of escrow instructions prepared by HW&S for the transfer

of one of the stores. The purported escrow named HW&S an escrow agent for the transfer., The escrow agreement, however, never became effective to create an escrow in HW&S with a fiduciary duty running to Flayac.

An escrow relationship ca only be created by contract. St. Paul Title Co. v. Meier, 181 Cal.App.3d 948, 952, 226 Cal.Rptr. 538, 540 (1986).[2] An escrow agreement requires the agreement of the grantor and the grantee to all the terms of the contract and acceptance by a third party (HW&S) of the position of depositary. House v. Lala, 180 Cal.App.2d 412, 4 Cal.Rptr. 366, 369 (1960); see also Security-First Nat. Bank of Los Angeles v. Clark, 8 Cal.App.2d 709, 712, 48 P.2d 167, 169 (1935) (essential characteristics of escrow must exist before escrow is created). Here, HW&S prepared the escrow agreement and sent it to the Humrichouses on March 12, 1984. In a cover letter, HW&S told the Humrichouses that the

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[2]All the events occurred in California. Therefore, California law applies.

document was a proposed escrow contract and asked its clients to review and, if necessary, revise it. In the letter, HW&S asked the Humrichouses to contact them when they wished to proceed with the escrow. HW&S was never contacted by the Humrichouses to proceed with the escrow. Rather, Flayac paid the 4700,000 installment on the purchase price of the stores the next day. The money was deposited into the GCD trust account held by HW&S. The GCD trust monies were, by agreement between Flayac and Humrichouses, available to the Humrichouses as of April 16, 1984. It is clear that the money was paid into the GCD account as partial payment for the stores and not paid pursuant to the proposed escrow arrangement. Because the document was never returned to them, HW&S never accepted the position of escrow agent. The $700,000 payment was made outside of any purported escrow arrangement.

Flayac also argues that HW&S owed them a duty as trustee of the $700,000 not to release the funds to the Humrichouses unless the sale of

the three stores obtained ARCO's approval. if HW&S was not Flayac's escrow agent, however, and if it had not otherwise acquired a fiduciary duty to Flayac, HW&S had no trustee relationship with him. The duty of HW&S ran only to the Humrichouses. When the $700,000 was paid into the GCD trust account maintained by HW&S, its duty concerning these funds ran only to the Humrichouses and not to Flayac. As the trial court noted, "[t]he source of the money is not determinative of the power of the trustee. That's defined by what the parties tell the trustee to do and in this instance by endorsing the CD, the parties irrevocably told Haines, Walker & Scott that the money was in trust for . . . GCD Investments". HW&S cannot be found liable to Flayac as either an escrow agent or as trustee.[3] The evidence only points to a duty of

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[3]Flayac argues that when an express trust fails because of impossibility a "resulting trust" with Flayac as beneficiary was created. The appellant's argument fails by its own terms. Here, no express trust was ever created. Rather, HW&S took the $700,000 in trust for its own clients the Humrichouses and not in trust for Flayac. Flayac was a third party to whom HW&S owed no duty.

HW&S to its own clients. There was no evidence of an escrow or trustee relationship between Flayac and HW&S. The trial court's directed verdict on this issue was proper.

II. Schwartz.

The trial court found that there was sufficient evidence of negligence on the part of Schwartz to take Flayac's malpractice claim to the jury. The court found that the April 16 agreement, prepared by Schwartz, because it did not provide for the return of Flayac's money if he wasn't approved by ARCO, potentially created liability in Schwartz.

However, the court limited Schwartz's potential liability to $700,000. The court found that Schwartz was not liable for anything that occurred after he went on vacation. Flayac argues that Schwartz should be liable for an additional $804,500 representing the amount "paid" for Howard Arlen, Inc. Flayac claims that Schwartz "recommended" that he buy Howard Arlen while knowing that it was a mere "corporate shell" without any assets. The trial

court, in ruling out Schwartz' liability for the $804,500, stated that the Howard Arlen transaction was a "nonissue". The court found that Howard Arlen was a "vehicle", a procedural method by which the underlying transaction was to be carried out. The court believed that the evidence indisputably showed that the $804,500 supposedly "paid" for Howard Arlen was nothing more than an allocation of part of the total purchase price and that no additional consideration in addition to the agreed $1.3 million dollar purchase price was made for Howard Arlen.

The Howard Arlen transaction was made pursuant to the May 15, 1984 agreement. Schwartz prepared a preliminary draft of the agreement and then sent it to HW&S for its review before he went on vacation. Schwartz' draft provided that the Wells Fargo escrow accounts containing the balance of the $1.3 million dollar purchase price remain open until Flayac was approved as franchisee by ARCO. HW&S then changed the agreement by deleting the

provisions providing for ARCO's approval of Flayac as franchisee. The HW&S draft, however, provided that the Wells Fargo escrows were to remain open.

Flayac and the Humrichouses then took the HW&S draft and further changed it. The version that was finally signed by the parties cancelled the escrows. It also provided that the escrows were to be reopened and were to remain open until Flayac qualified with ARCO. Flayac then took the money from the cancelled escrows and gave it to the Humrichouses outside of escrow.

It is clear that the agreement that the parties finally signed was materially different from that which Schwartz prepared. The manner of payment of the balance of the purchase price was completely different from that contemplated by Schwartz. It also took place while Schwartz was not present. He cannot be liable for any damage to Flayac related to the May 15 agreement. He is only potentially liable for the $700,000 transferred from Flayac to the

Humrichouses pursuant to the April 16 agreement.[4]

III. Setoff.

Flayac and the Humrichouses settled out of court for some $650,000. Five hundred thousand dollars of the settlement consisted of a promissory note given to Flayac, at 10% interest, payable in four years. The trial court set off the amount of any recovery against Schwartz by the $650,000 face value of the settlement. Flayac argues that the proper valuation of the note is its market and not its face value.

Cal. Civ. Proc. Code Section 877 (West

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[4]Flayac at trial testified that Schwartz told him to "rely on McMaster" (an attorney at HW&S) in regards to the Howard Arlen transaction when Schwartz was on vacation. The trial judge found it difficult to believe Flayac's testimony; "I realize Mr. Flayac has said that Mr. Schwartz told him he could rely on Mr. McMaster. I just view that testimony as being like testifying that the sun comes up in the west and goes down in the east..." Schwartz denied making the statement.

It seems that the district judge improperly rejected the nonmoving party's testimony as to a material fact. The trial court, however, expressly disavowed that it based its ruling on the disputed testimony. Rather, it stated that its basis of decision was Schwartz' absence at the time the transaction was consummated and the material changes in the draft Schwartz prepared.

1980), controls the issue of the value of the settlement. Section 877 provides:

> Where the release, dismissal with or without prejudice, or a covenant not to sue or not to enforce judgment is given in good faith before verdict or judgment to one or more of a number of tortfeasors claimed to be liable for the same tort --
>
> (a) It shall not discharge any other such tortfeasor from liability unless its terms so provide, but it shall reduce the claims against the others in the amounts stipulated by the release, ... or in the amount of the consideration paid for it whichever is the greater.

By its terms, Section 877 requires setting off the face value of the amount stipulated by the release. The release provided for the transfer of some real property of the Humrichouses worth approximately $150,000. The worth of the property is not at issue here. The release also incorporated by reference the amount of the promissory note -- $500,000.

The appellant points to Franck v. Polaris E-Z Go Div. of Textron, 157 Cal.App.3d 1107, 204 Cal.Rptr. 321 (1984) and In re Marriage of Tammen, 63 Cal.App.3d 927, 134 Cal.Rptr. 161

(1976), to support his argument that the market value of the promissory note should be set off and not its face value. In Franck, the settlement provided for payments over a seventeen year period. The court noted that the money to be received by the plaintiff at the end of the seventeen year period would not be worth as much as the same amount of money received immediately. Thus, only by discounting the future payments to present cash value and reducing the award by only that amount, would the plaintiff receive the amount to which she was presently entitled. Franck, 157 Cal.App.3d at 1117, 204 Cal.Rptr. at 326.

In Tammen, a court-ordered community property division awarded the wife 79% of the couple's property. To equalize the division, the judgment also ordered her to execute a ten year interest bearing promissory note to the husband. The court addressed the issue of whether, as a matter of law, the promissory note was worth substantially less than its face value. Tammen, 63 Cal.App.3d at 931, 134

Cal.Rptr. at 163. The court noted that the security had market value which, in this case, was affected by

> the inferiority of its security, the long and uncertain deferment of its enjoyment, the probable effect of inflation upon it, and the concerns of its ownership. We share the common knowledge, and accordingly take judicial notice ... that it would at least be worth substantially less than its face value.

Id. The appellant's argument based on Franck and Tammen is unpersuasive.

First, Tammen is not on point because it addresses an issue unique to the community property area -- equal division of property. Also, Franck refers not to the "market value" of promissory notes but to their "present cash" value. Present cash value represents the amount of a note at any particular time less the interest not yet accrued. Market value is a much more nebulous figure reflecting the amount that the note could be sold for at any particular time. Most importantly, the promissory note in the case at bar is only a four year note. It carries a generous interest

rate (10%). The rate serves to protect Flayac from any future loss of value of the money tied up in the four year settlement.

Flayac also argues that the trial court erred in settling off the value of the Rincon store against any potential liability in Schwartz. Caudle was approved by ARCO as franchisee of the Rincon store. Flayac later rescinded the Rincon store transaction and "delivered" the store back to the Humrichouses. Eventually, ARCO took possession of the store from them. The trial court ruled that, because Flayac obtained at least a third of what he bargained for, any damages he might obtain should be set off by the purchase price of the Rincon store. Flayac argues that the deal was made for all three stores and if all three stores were not delivered he did not receive the benefit of his bargain. The trial court is correct. Flayac obtained full possession of the Rincon store. It was operable as an independent unit. Accepting Flayac's argument would mean he would collect a wind-fall if he received in

damages the full $1.3 million dollars he claimed. He would receive the $1.3 million plus an additional $350,000 representing the value of the Rincon store.

IV. Punitive damages.

Flayac argues that if the case had gone to the jury Schwartz could have been found liable for punitive damages. Under California law, punitive damages may be obtained "in an action for the breach of an obligation not arising from contract, where the defendant has been guilty of oppression, fraud, or malice, the plaintiff, in addition to the actual damages, may recover damages for the sake of example and by way of punishing the defendant." Cal. Civ. Code section 3294(a) (West 1987).

Punitive damages must be based on more than a simple breach of fiduciary duty. Malice or actual fraud must be found; mere negligence or recklessness will not suffice. Mihara v. Dean Whitter & Co., 619 F.2d 814, 825 (9th Cir. 1980) (construing Cal. Civ. Code Section 3294(a)). See also, Hillard v. A.H. Robins Co.,

148 Cal.App.3d 374, 392, 196 Cal.Rptr. 117, 128 (1983) (conscious disregard may constitute malice). At trial, the appellant never proved anything but negligence on the part of Schwartz. There is no proof of any malice or actual fraud on the part of Schwartz in the record. A directed verdict on the punitive damages issue was proper.

V. Conspiracy.

Prior to trial, the court provisionally excluded any evidence of "conspiracy" between HW&S and Schwartz to defraud Flayac. The judge ordered the appellant make an offer of proof of any evidence of conspiracy. There is no indication in the record that an offer was ever made. Fed. R. Evid. 1039(a) provides that

> Error may not be predicated upon a ruling which admits or excludes evidence unless a substantial right of the party is affected, and.... In case the ruling is one excluding evidence, the substance of the evidence is made known to the court by offer....

Because no offer was ever made, the appellant is precluded from raising the conspiracy issue on appeal.

CONCLUSION

We AFFIRM. The trial court properly found that no escrow or trustee relationship existed between HW&S and Flayac. As a matter of law, Schwartz is not liable for any damages to Flayac related to the May 15, 1984 agreement. The trial court also properly set off the face value of the promissory note rather than the market value of the note. The appellant also failed to prove any facts warranting an award of punitive damages. The court awards costs to the appellees.

FLETCHER, Circuit Judge, Concurring in part and Dissenting in part:

I concur in parts I, IV and V of the majority's disposition, nd in that portion of part III holding that the setoff value of the note was properly calculated. I cannot, however, join in part II or the portion of part III dealing with the Rincon store setoff. I think it obvious that the district court erred in taking from the jury the question of Schwartz's liability for negligent representation. Further, the court erred in thinking that Flayac derived any benefit from the Rincon store.

If the plaintiff is believed, Schwartz knowingly and falsely represented in the contract he drafted that Howard Arlen, Inc. was a holding company for two of the ARCO stores. While it is true that Schwartz left for vacation before the draft agreement was signed, and that the agreement was substantially revised after he left, it seems unlikely that Flayac would have signed <u>anything</u> had Schwartz not told him and

represented in the draft agreement that Howard Arlen, Inc., owned the ARCO stores. Since we are reviewing a directed verdict, we must construe all the evidence in the light most favorable to Flayac. The plaintiff adduced credible evidence that (1) Schwartz knew Howard Arlen did not own the ARCO stores; (2) Schwartz knew that Flayac's reason for buying Howard ARlen was that he thought he would acquire beneficial ownership of the stores by that means; (3) Schwartz's representations that Howard Arlen was the holding company for the two stores caused Flayac to buy Howard Arlen, and (4) in fact, Howard Arlen was an empty corporate shell. Despite this strong factual showing, the district court directed a verdict in favor of Schwartz.

Indeed, the district court agreed that "there was sufficient evidence against Schwartz to go to the jury." But, inexplicably, after hearing arguments from the attorneys on whether to direct a verdict, it dismissed the possibility of liability arising from the Howard

Arlen transaction as "kind of a non-issue". The court offered the following rationale:

> [I]t really doesn't make any difference. The essence of the plaintiff's agreement here; that is, he was going to buy three stores for 1.3 million, and Howard Arlen, whatever it was and whatever it was not, went along with it; and that the breach of Humrichouse agreement to give Mr. Flayac what he though he was getting was really in conveying the operating entity, the stores, and not Howard Arlen.
>
> [I] don't believe there is any evidence that Mr. Flayac paid any money or agreed to pay any additional consideration for Howard Arlen at all.

Flayac's attorney objected to the court's conclusion, arguing that Howard Arlen was not a non-issue, but the vehicle by which the Humrichouses, to avoid the necessity of ARCO's approval, tried to transfer ownership of two of the ARCO stores to Flayac, a non-citizen. "When Mr. Flayac bought Howard Arlen, Inc., stock, he though he was, in effect, buying the corporation that owned the right to the two stores, the holding company," counsel said. The court responded by saying that such representations

did not matter because it was the failure to obtain the stores, and not what Flayac thought about Howard Arlen, that injured Flayac. "He was going to pay his money anyway," the court said. Counsel retorted, "He wasn't going to pay until he got evidence of ownership. So the evidence of ownership in this case was the Howard Arlen stores, which turned out not to be, and his own attorney knows it wasn't." Schwartz admitted at trial that he knew Howard Arlen did not own the stores, but nonetheless used the name "holding company" as a convenience. The draft of the contract prepared by Schwartz stated:

> "WHEREAS, the corporation HOWARD ARLEN, INC. has been formed as a holding company for certain AM/PM MINI MARKETS as further described in this agreement;..."
>
> (Emphasis added)

Indeed, Haines, Walker & Scott argues in its brief that the "undisputed evidence established that Haines, Walker & Scott informed Flayac's attorney Schwartz and Schwartz understood that Howard Arlen, inc. was a

management company and did not 'own' the franchises for the two stores." Haines Brief at 33. (Emphasis added.) Schwartz, in his brief, does not deny having known that Howard Arlen owned nothing; he, instead, makes the same argument the district court made -- that the acquisition of Howard Arlen cost Flayac no money beyond what he was prepared to pay for the ARCO stores. Schwartz Brief at 31-33.

The court conceded that "the evidence can reasonably be construed ... that Mr. Flayac believed, based on action by the lawyers, that Howard Arlen was a holding company, and Howard Arlen didn't end up holding anything." Despite this concession the court directed a verdict against Flayac.

Changes in the wording of the agreement made in Schwartz's absence may have insulated Schwartz from liability for damages arising from the changed wording or new terms of the signed agreement, but the jury could nonetheless have found Schwartz liable for misleading Flayac into buying Howard Arlen under any terms. In fact,

during argument on the motions for directed verdicts, Flayac's attorney pointed out that "Schwartz adopted the language which Mr. Flayac understood to be giving him beneficial ownership of the stores.... Mr. Schwartz put that into the contract." When the court responded that Schwartz's first draft had later been "chopped to pieces", Flayac's attorney said, "No, dir. Not that part. That part stayed right in there... [A]ll the lawyers left that in there, including Mr. Schwartz when he got back from vacation." Clearly the jury should have made the decision as to Schwartz's ultimate responsibility.

I also cannot agree that the trial court's setoff of $350,000 because Flayac received the Rincon store was proper. The majority states that "Flayac later rescinded the Rincon store transaction and 'delivered' the store back to the Humrichouses. Eventually, ARCO took possession of the store from there." it then erroneously concludes that, "because Flayac obtained at least a third of what he

bargained for, any damages ... should be set off by the purchase price of the Rincon store .... Accepting Flayac's argument would mean he would collect a wind-fall if he received in damages the full ... $1.3 million plus an additional $350,000."

Flayac would receive a "windfall" only if his $350,000 had been returned to him. It was not. Flayac's attempted rescission did not restore him to his prior position -- he never received his money back.

The district court erred in taking the issue of Schwartz's liability from the jury. The majority has erred in perpetuating the error.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

BERNARD FLAYAC, No. 87-1553

Plaintiff-Appellant,

vs. D.C. No. CV-85-1363-CAL

CRAIG ALLEN HUMRICHOUSE, et al.,

Defendants.

and

JAMES G. SCHWARTZ, individually; STALEY, YOUNG & SCHWARTZ, a professional corporation; HAINS, WALKER & SCOTT, a law partnership,

Defendants-Appellees.

Before: FLETCHER, WIGGINS, NOONAN, Circuit Judges

Appellant's petition for rehearing is denied. Judge Fletcher dissents.

Filed: October 6, 1988
U.S. Court of Appeals

EXHIBIT "B"

DECLARATION OF SERVICE BY MAIL

I declare that:

I am a citizen of the United States and employed in Contra Costa County, State of California, over the age of eighteen years, and not a party to the within action. My business address is 18 Crow Canyon Court, Suite 395, San Ramon, California 94583.

I served the foregoing

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF
APPEALS FOR THE NINTH CIRCUIT
(Reformatted Copy)

by depositing THREE COPIES to each counsel addressed below, in the United States mail at San Ramon, California, enclosed in a sealed envelope, with postage thereon prepaid, addressed as follows:

Long & Levit
101 California Street, Suite 2300
San Francisco, CA. 94111

Lillick, McHose & Charles
Two Embarcadero Center
San Francisco, CA. 94111

Executed at San Ramon, California and deposited in the United States mail on February 15, 1989.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Jane A. Curtis

Jane A. Curtis